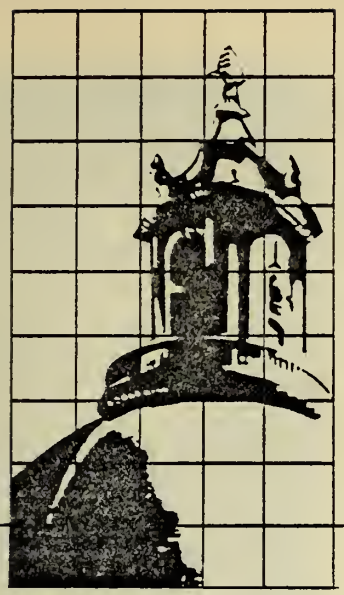
BLUEPRINT FOR REFORM

STATE AUDITOR'S OFFICE
JOHN J. FINNEGAN, AUDITOR



Blueprint For Reform:
A System for the Purchase of Services

STATE AUDITOR'S OFFICE

JOHN J. FINNEGAN,
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A Message from the State Auditor

Despair, economic depression, isolation, and family trauma face a growing segment of the clients served by the Commonwealth's social and rehabilitative services network.

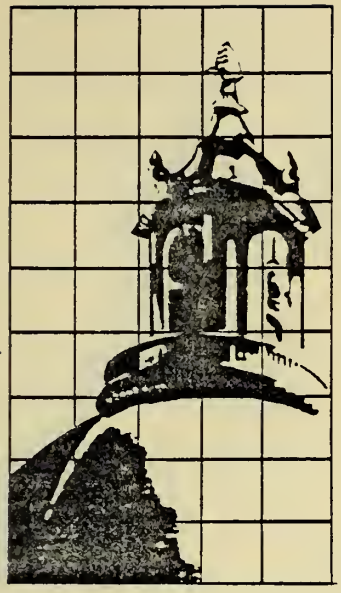
Because human services must be properly planned, administered and delivered, my office has prepared the Blueprint for Reform, a comprehensive analysis of the social services delivery system that identifies structural weaknesses in the state's method of purchasing services and recommends reforms to correct mismanagement.

Reviews of seven state agencies and audits of 122 providers disclosed areas of mismanagement totalling $19.3 million in fiscal year 1983 alone. Clearly, programs that the state purchases must be cost reconcilable to safeguard tax dollars and to ensure services delivery to needy clients.

An unprecedented step for this office is the establishment of an institute to train members of the human services community in areas of finance and management. Institute training coupled with follow-up audits and Blueprint reforms will help ensure economy and efficiency in the delivery of human services.

Sincerely,

John J. Finnegan
Auditor of the Commonwealth



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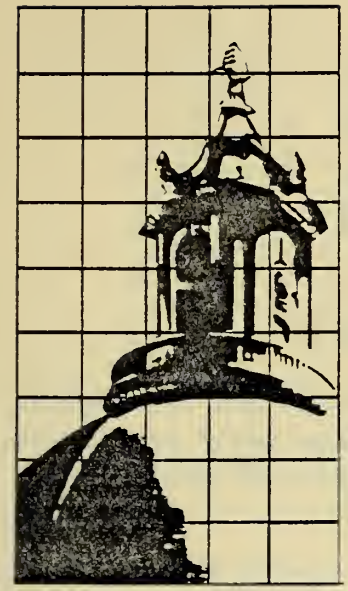

Chapter I
Historical Synopsis: Purchase of Services

The current method of purchasing social and rehabilitative services in Massachusetts resulted from the massive growth during the 1970s of community-based human service programs. In 1971, the Commonwealth expended approximately $25 million for purchased services. By 1979, the figure had risen to $185 million. In fiscal year 1983, the Commonwealth expended more than $372 million for purchased services (see Exhibit 1, p. 3).

Several factors contributed to the significant growth of purchased services. First, thousands of state clients were transferred from state institutions to community-based programs. Second, the Commonwealth entered into consent decrees that resulted in the population at state facilities being further reduced and additional community-based services being purchased. Third, federal and state legislative actions provided incentives for the Commonwealth to purchase social and rehabilitative services from the private sector.

Specifically, two major agencies contributed the most to the growth of purchased services: the Department of Youth Services (DYS) and the Department of Mental Health (DMH). The movement of youth offenders from DYS reform schools to residential detention and treatment centers resulted in major decreases in the number of juveniles treated at DYS institutions. As the population of juveniles in institutions decreased, the purchase of community-based services increased. In fiscal year 1970, 507 juveniles were in DYS institutions; by March 1973, that number had been reduced to 17.[1]

Treatment philosophies also changed in mental health. Consequently, the Commonwealth administratively reorganized the Department of Mental Health (DMH). A vast and complex

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[1]Richard B. Hill, Thinking Systematically About Purchasing Social Services (Boston: Commonwealth of Massachusetts Rate Setting Commission, 1982).

community-based network of mental health and retardation service providers emerged. The average daily population at the state hospitals was reduced from 15,168 patients in 1967 to 1,875 patients in 1982.[2]

The movement of patients from state institutions to community settings (deinstitutionalization) was fueled by a series of lawsuits resulting in consent decrees entered into by the Commonwealth. The first such class action was filed in 1972 on behalf of the clients of Belchertown State School. This lawsuit charged the state with operating an overcrowded, understaffed, unsanitary, and unnecessarily restrictive treatment setting. The Commonwealth entered into the Belchertown consent decree in November 1973. Consent decrees were later entered into for the Monson, Walter E. Fernald, Wrentham, and Paul A. Dever State Schools and for Northampton State Hospital. As a direct result of these consent decrees, census figures at state hospitals fell significantly as residents were moved to noninstitutional, community-based programs.

Several federal and state legislative actions contributed to the expenditure growth for purchased services. On the federal level, these actions included (1) the Community Mental Health Center Act, which authorized construction of clinical facilities to provide a full range of inpatient and outpatient services for the mentally retarded; (2) the 1967 amendments to the Social Security Act, authorizing federal reimbursement for up to 75% of state expenditures on services purchased from for-profit and nonprofit providers; (3) the 1969 amendments to the Social Security Act, allowing privately donated funds to be substituted for state funds in matching federal social service grants; and (4) the 1974 amendments to the Social Security Act (Title XX), which made contracts between the state's social service agencies and private providers an eligibility requirement for federal reimbursement.

On the state level, legislative actions contributing to the increase in purchased services included the 1966 passage of

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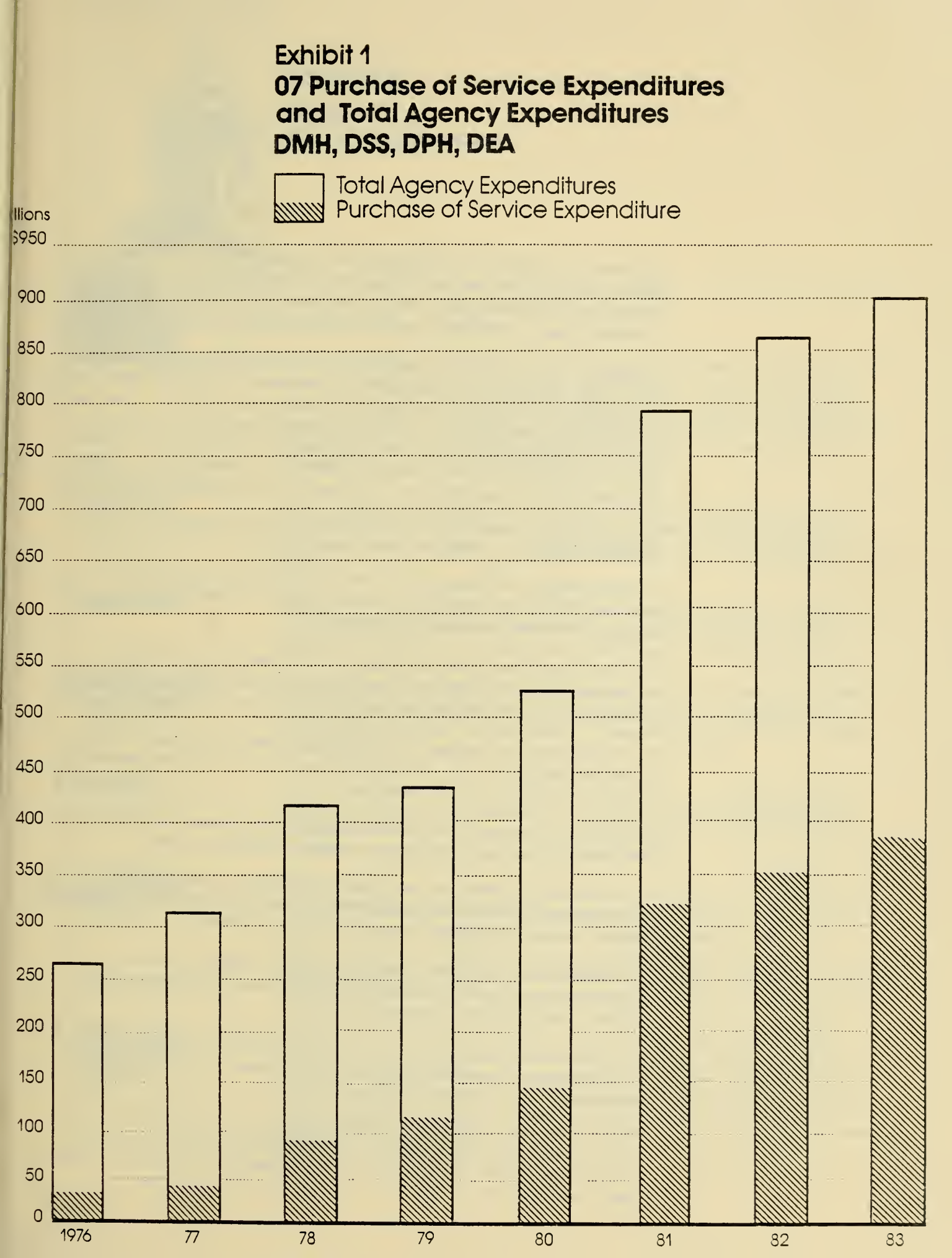
[2] Massachusetts Department of Mental Health, Average Daily Census by State Hospital: 1960-1982 (Boston, 1983).

Exhibit 1
07 Purchase of Service Expenditures and Total Agency Expenditures DMH, DSS, DPH, DEA



Chapter 735, which established a comprehensive program of mental health and mental retardation services, and the 1970 passage of Chapter 888, which revised the laws pertaining to admitting, treating, and discharging of the mentally ill.

Although the important factors in the growth of purchased services--deinstitutionalization, consent decrees, and legislative and regulatory changes--are identifiable, the more fundamental question of whether to purchase services or to provide them directly is not as easily addressed. However, social researchers and commentators have asserted a number of generally accepted pros and cons of purchased services.

The principal advantages of purchased services most frequently cited in reports and studies are:

1. Purchased services are less expensive than direct service delivery when per-client institutional and community-based costs are compared.

2. Purchased services are more efficient than direct service delivery because they can be provided without the intervention of costly governmental bureaucracy.

3. Purchased services are of higher quality than direct service delivery due to private sector's program expertise and personnel specialization.

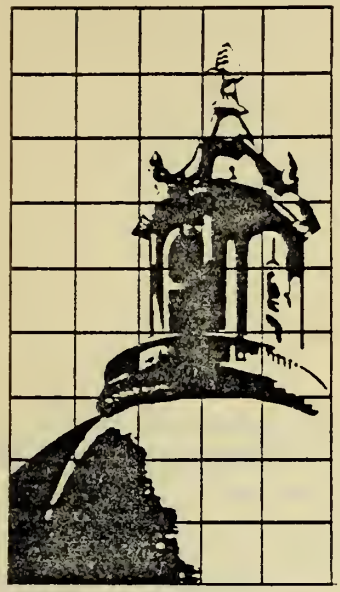
Similarly, several disadvantages of purchased services are frequently cited. The most common arguments are:

1. Purchased services are more expensive than direct service delivery when management, monitoring, and oversight costs by governmental agencies are included.

2. Purchased services are difficult to manage since governmental agency personnel often specialize in areas other than contract administration.

3. Purchased services lack accountability because governmental agencies do not have direct control over personnel and service delivery.

While the aforementioned advantages and disadvantages to purchasing services exist, our careful analysis has revealed that the Commonwealth's purchase-of-service experiment has failed to realize any of the advantages.



Chapter II
Digest of Major Deficiencies

Our examination of the Commonwealth's current method of purchasing services encompassed audits of 122 provider agencies, 4 state purchasing agencies, and 3 state regulatory agencies. The Blueprint for Reform addresses the following deficiencies and recommends specific actions designed to create an accountable purchasing system:

1. Standards

The current method of purchasing services is characterized by confusing, conflicting and fragmented agency-specific standards, regulations, policies, and reporting requirements.

2. Regulations

State purchasing agencies develop and promulgate conflicting and overly complex regulations which result in providers' inability to operate consistently and effectively.

3. Geographical Boundaries

State purchasing agencies currently maintain separate, noncorresponding geographical boundaries that contribute to the fragmentation, duplication, confusion, and inefficiency of the current method of purchasing services.

4. Planning

Due to fragmented, inadequate, informal, or nonexistent statewide needs assessments by state purchasing agencies, public funds may be expended for vacant slots in contract programs, and services may be duplicated.

5. Rate Setting Process

The present rate setting process is unwieldy; the Rate Setting Commission (RSC) currently establishes class rates, unit rates for individual provider's contracts and programs, maximum allowable rates, approved budgets for cost reimbursement contracts and programs, class rates with minimum and maximum levels, and rates for individual clients.

6. Integrated Automated Systems

The state's current method of purchasing services is not sufficiently automated, nor does it ensure integrated systems for data gathering, model assimilation, program and fiscal decision-making and processing. In addition, existing automated systems are not sufficiently protected from unauthorized access.

7. Contract Cycle

The current method of purchasing services operates on a 12-month cycle that coincides with the fiscal year (July 1 - June 30). All purchase-of-service agreements (AF-7s) technically expire on June 30, resulting in thousands of contracts to be hastily negotiated and rushed through the renewal process to meet the June 30th deadline.

8. Contract Language

Contract provisions and requirements vary from one agency to another; 07 contracts include general terms and conditions, contract language, and multiple attachments, which are difficult to understand, often ambiguous, and sometimes in conflict with those of other purchasing agencies.

9. Performance Contracts

State purchasing agencies operate independent purchase-of-service programs with varying contractual/noncontractual arrangements. Many contracts do not contain measurable goals and objectives such as performance standards for program evaluation.

10. Multiple Service Contracts

The current method of purchasing services results in multiple contracts between state purchasing agencies and providers that supply a particular service, voluminous paperwork, and burdensome contract procurement and administration procedures that vary among agencies.

11. Standard Accounting and Record-Keeping Practices

Of the 1,100 providers that contract with numerous state purchasing agencies, many do not use standard accounting and record-keeping practices, resulting in insufficient accountability and control.

12. Client Funds

State purchasing agencies do not adequately monitor providers' controls for the safeguarding of, and accounting for, clients' funds.

13. Interest Payments and Untimely Reimbursements

Provider agencies assert that they experience cash flow problems due to program start-up and untimely fiscal year-end state payments; consequently, many providers borrow money at high interest rates from commercial lending institutions.

14. Reimbursement for Vacant Contract Slots

As a result of past contract policy, the Commonwealth reimburses providers for empty beds or vacant slots.

15. Surplus Income

The current method of purchasing services does not ensure that the state is paying only for the cost of those services actually rendered.

16. Real Property

Inadequate controls and oversight mechanisms and improper contract procurement and administration practices in general have resulted in the Commonwealth reimbursing providers (or related parties) for mortgage costs incurred in purchasing real property.

17. Purchase and Inventory of Furniture and Equipment

The process by which providers contracting with state agencies purchased furniture and equipment with public funds was inadequate and did not allow for accountability.

18. Client Records

Contract conditions used by most state purchasing agencies allow providers to retain client information and records upon contract termination, resulting in state forfeiture of valuable data.

19. Precontract Provider Qualifications

No formal, statewide precontract qualifications exist for providers of social and rehabilitative services.

20. Conflict of Interest

Purchase-of-service agreements between state agencies and providers are not properly monitored to prevent potential conflict-of-interest situations.

21. Training for Contract Personnel

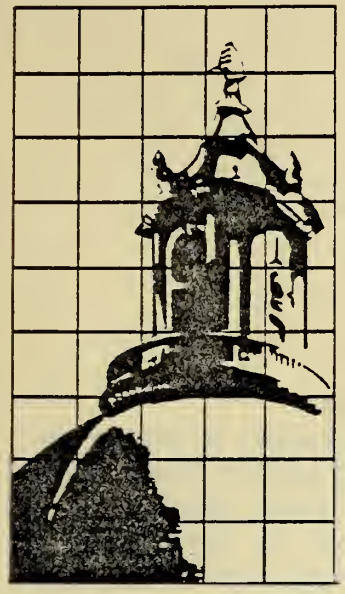
The Commonwealth has provided little or no training in contract negotiation and financial management to area and regional staff involved in purchase-of-service procurement and administration.

22. Contract Monitoring

Due to insufficient and inadequate contract monitoring by state purchasing agencies' area and regional offices, providers' compliance with fiscal and programmatic contract provisions is not ensured.

23. Contract Enforcement

Purchasing agencies currently have insufficient and inadequate policies and mechanisms for enforcing laws, regulations, and contract conditions pertaining to providers' unacceptable or incomplete fulfillment of contract provisions and delivery of contract services.



Chapter III
Blueprint For Reform A System for Purchasing Services

A. Introduction

The following overview describes a simple, effective, and manageable purchasing system. To remedy the currently deficient purchasing method, our proposed system identifies three critical elements of effective management: centralized control, statewide planning, and performance reporting.

Centralized control, an oversight function, ensures that state agencies are using resources effectively; are following applicable, prescribed policies and procedures; and have clearly defined responsibilities within the purchasing system. Planning, which is based on systematic needs assessment and allocation of available resources, establishes statewide contract procurement and administration goals, objectives, policies, procedures, and performance standards. Performance reporting documents the state's and the provider agencies' actual progress toward achieving predetermined goals, objectives, and performance standards; and measures agencies' compliance with policies and procedures.

The links between and among these components are formal and informal communication channels that foster the multidirectional flow of timely, accurate, and needed information for effective, efficient, and accountable management.

A comprehensive purchase-of-service system must contain two distinct functions: contract procurement and contract administration. Our proposed system articulates certain practices and principles--accountability, standards, and responsibility--which must apply to both functions to ensure control, planning, and efficiency.

Furthermore, our proposed system defines and separates contract procurement and contract administration. Procurement includes all activities beginning with the establishment of standards through the signing of the contract. Administration begins after the signing of contract and ends with the expiration of the 12-month contract period.

B. Contract Procurement

For a comprehensive, statewide purchasing system to be effective, standards, regulations, and policies must be cen-

trally planned and promulgated. Furthermore, a statewide purchasing system must have one central entity responsible for ensuring statewide compliance with these standards, regulations, and policies. These tasks will be best accomplished by the Executive Office for Administration and Finance (EOAF). (see Recommendation 1, p. 16) As the executive office charged with the responsibility of central planning, financial administration, and program and policy coordination, EOAF is already mandated to perform this critical function. EOAF can provide for proper planning, standards, and control by establishing the following:

- Criteria for decision to purchase or directly deliver services;
- Standard statewide agency geographical boundaries for service delivery;
- Standard program and service models for all categories of purchased services;
- Regulations that are compatible among agencies;
- Standard contract format;
- Standard procurement process; and
- Accessible and centrally-operated automated data processing and management information systems that are compatible among agencies.

Our proposed purchase-of-service (POS) system suggests that the contract procurement and administration functions must be performed independently of whether the method of purchasing services is centralized (as in the Department of Elder Affairs) or decentralized (as in the Department of Social Services). In a centralized agency, procurement and administration must be performed by two separate divisions within the central office. In a decentralized agency, procurement must be assigned to one agency level, i.e. the regional/district level, while administration must be assigned to another agency level, i.e. the area level.

Our proposed system is flexible, but one important principle is that contract procurement and administration must be segregated.

Following the establishment of standards, the next activity in the contract procurement function must be service needs assessments. The purchasing agency's regional/district offices must perform such needs assessments according to the standards established by the Executive Office for Administration and Finance (EOAF). The agency's central office--along with the executive office--must ensure compliance with, and enforcement of, contract procurement policies and procedures.

Following such assessments and the identification of actual service needs, the purchasing agency's central office decides, according to the standards that EOAF promulgates, whether to best meet the service need through purchasing or through direct provision. The regional/district office should be responsible for the allocation of the budget among those services which it purchases.

If the services are to be purchased, the purchasing agency's regional office must develop and issue a standard request for proposal (RFP), which must adhere to the standards that EOAF develops. The RFP must contain a detailed description of the purchased service, as well as the nonnegotiable precontract qualifications (see Recommendation 19, p. 47). EOAF develops these qualifications, and all providers bidding for contracts must conform to the qualifications as a condition of contracting. All providers, for example, must demonstrate responsible management and fiscal capabilities in addition to programmatic expertise.

The next activity in the procurement function must be evaluating and selecting proposals for given programs and negotiating contracts. The area office shall evaluate and select proposals, and the regional office must approve them. Once proposals are selected, standard contracts that the regional office prepares must then be grouped and negotiated on the regional level according to a service category. (For example, if a given region had 10 areas, each with new alcohol rehabilitation programs to be purchased, negotiation for contracts in all 10 areas would be coordinated regionally.) This would streamline the current practice of establishing contract rates based on six different procedures.

The Rate Setting Commission (RSC) should be a pricing board, establishing "cost corridors" (minimum and maximum rates) for service models based on historical cost data (See Recommendation 6, p. 26). The RSC must also be responsible for projecting future cost trends for various service categories. Purchasing agencies shall use the cost trends for budget projections.

As a condition of contract award, providers must sign an affidavit of compliance in which both the state agency and provider recognize and agree on reporting and filing requirements (see Recommendation 19, p. 47) and legal sanctions for incomplete, fraudulent, or otherwise unsatisfactory performance of contract provisions (see Recommendation 23, p. 53). The purchasing agency will initiate the AF-7 (see Glossary). When the AF-7 is approved by the purchasing agency, executive office, and the Comptroller, it is date-stamped and the contract takes effect.

The Commonwealth must also adopt a new contract document for purchased services. The new contract must contain performance factors that can be used to evaluate the quality of the service and the compliance with the terms of the contract (see Recommendation 9, p. 32). The performance factors may include (1) client attendance; (2) client/staff ratio; (3) cleanliness of facility; and (4) the level of revenue generation (medical assistance, client fees, and third-party insurance). Special contract provisions should be established for start-up and phase-down contracts (see Glossary).

C. Contract Administration

Contract administration (monitoring, evaluation) must begin on the date the contract takes effect. In a centralized agency, contract administration must be performed by a separate division within the central office. In a decentralized agency, this function must be performed at the agency's area offices. Area directors must be held responsible for submitting to regional offices monthly reports on the area office's monitoring of contract compliance. Providers shall be required to submit standard monthly reports on quality assurance, expenditures, and client vacancies to the central office's contract administration division or the area office. Agency area offices or central office's

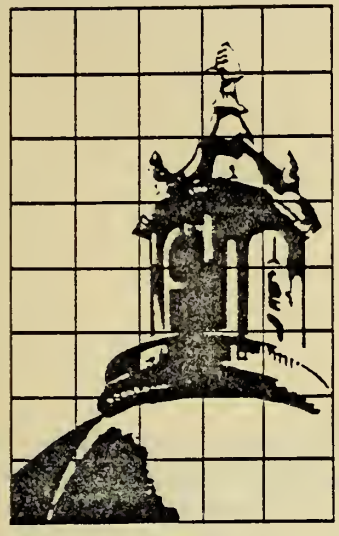
administration divisions must monitor the budget and provide control and quality assurance through the following activities:

- Monitoring the program by filing monthly reports and performing on-site reviews based on standards that the central office develops;
- Pre-auditing all invoices before payment;
- Evaluating monthly expenditure reports;
- Evaluating monthly vacancy reports;
- Monitoring compliance with contract terms; and
- Reconciling the budget with expenditures.

In decentralized agencies, the area office, while maintaining primary contract program administration responsibilities, must share with the regional/district office the financial management and payment responsibilities. After reviewing certain reports (as cited above) and pre-auditing all invoices which the provider submits with supporting documentation to ensure that the clients served were identified by program and contract, the area office will submit a payment authorization order to the regional office. Using the Comptroller's Advance Payment System (see Glossary), the regional office will process payment for the provider and maintain responsibility for the Return of Advance (see Glossary) function. Before the final invoice is submitted, the provider must reconcile revenues with expenses to ensure that the final invoice reflects only allowable costs for services actually rendered under the particular contract for that contract year. The area office must certify the invoice and submit to the regional office a final payment authorization for processing. Reconciliation must be verified when audited. The purchasing agencies' central offices must monitor the regional/district offices to ensure that they are adhering to the monitoring procedures established for them. In a centralized agency, a similar process should be performed by the contract administration division.

Our purchase-of-service system addresses the critical elements of planning, standards, accountability, control, and efficiency that are lacking in the current purchase-of-service method. We recognize that situations such as statewide contracts exist in the present purchase-of-service method that may not conform to our proposed system. Further, we recognize that some state agencies have assigned contract procurement and administration functions to organizational levels which differ from our model. However, these exceptions do not detract from the overwhelming need for planning, standards, accountability, control, and efficiency.

The Findings and Recommendations (Section IV), as well as the Table of Contents, are not presented in order of the seriousness of the deficiencies. Rather, these items are organized by function--contract procurement followed by contract administration. It is our belief that the Commonwealth must first design the system and pour the foundation before it frames the structure for a comprehensive purchase-of-service system.



Chapter IV
Findings and Recommendations

1. Standards Deficiency

Planning and promulgating of standards, regulations, and policies on a statewide level for procuring and administering purchased services are currently inadequate and fragmented. This has resulted in confusing and conflicting standards, regulations, and policies since each purchasing agency creates its own POS subsystem. These subsystems lack uniformity and standards, often resulting in duplicated services and inefficient expenditure of public funds.

Although the Commonwealth has been purchasing services for more than a decade, no central bureau has ensured that uniform standards, management controls, planning criteria, and compliance reporting existed. The Commonwealth has no criteria upon which to determine when services should be more appropriately purchased from the private sector rather than provided directly by the state. Nor has the state systematically evaluated the cost-effectiveness of either method of service delivery.

Examples

1. One centralized state purchasing agency with contracts in excess of $75 million consistently failed to solicit competitive bids for its contracted services, in violation of 801 CMR 25.04. Our review indicated that this practice resulted from the agency's interpretation of the contract procurement process, which varied from most other state purchasing agencies' interpretations.

2. We audited one provider that operated two similar programs that were each funded by two contracts with two purchasing agencies. One contract was unit rate; the other was cost reimbursement. The provider, which we cited for numerous deficiencies, not only had to operate under the two purchasing agencies' differing standards and reporting requirements but also had to administer two different types of contracts.

3. The Departments of Mental Health, Social Services, Public Health, and Elder Affairs purchase respite care, a service providing temporary relief to families with physically or mentally disabled adults or children living at home. The lack of statewide planning, coordination, and standards

results in a situation in which a provider that contracts with more than one of the above-mentioned agencies has varying reporting requirements and a variety of reimbursement rates. From a client's perspective, the lack of coordination among agencies often results in the client being moved among agencies before he or she secures the needed service. Furthermore, although the extent of duplicated services among these four agencies is unknown, one agency alone has estimated that duplication of services occurs in 25% to 50% of its caseload.

Recommendation

The Executive Office for Administration and Finance (EOAF) must formalize a central entity to improve performance of its mandated responsibilities. Centralizing control in this fashion will ensure proper management, uniform standards, accountability, and coordination within a purchase-of-service system. Strengthening an entity such as the Purchase-of-Service Policy Group (POSPG), established in 1983 by EOAF, may accomplish this critical task. (See Recommendation 6, p. 26) In any case, EOAF must coordinate the development of a statewide purchase-of-service evaluation plan which will provide needed information about program cost-effectiveness on a systematic basis. EOAF must--

- Establish a comprehensive inventory of all services provided by the public sector and those purchased from the private sector;
- Determine which categories or classifications of services should be purchased from the private sector and which services should be provided directly by the Commonwealth, and the cost-effectiveness of both methods;
- Establish standards for service procurement, such as needs assessments, requests for proposals, precontract provider qualifications, selection criteria;
- Train state personnel in contract negotiation, budgeting, administration, and evaluation;
- Establish standards for contract operations, including uniform contract documents, uniform client-specific forms (including intake and referral), and uniform payment processing procedures;

- Establish standards for contract administration, such as monitoring, reporting, and evaluating--including planning for statewide automated systems; and

- Establish and implement procedures for monitoring state agencies' adherence to regulations and standards governing service procurement and contract administration.

Centralizing control within EOAF will not require additional state funding since the personnel and expertise currently exist within the secretariat and purchasing agencies. Sufficient personnel exist whose backgrounds and experience should encompass expertise in areas such as business administration, public administration, government, or law. All of these personnel should have experience in contract procurement and administration, as well as demonstrated experience in management, coordination, and negotiation.

The Executive Office for Administration and Finance (EOAF) should be assisted, on an ad hoc basis, by senior staff from each executive office involved in the purchase of services and one senior staff person from each purchasing agency. These personnel should have programmatic as well as financial experience in the purchase of services.

2. Regulations Deficiency

Purchasing agencies often have conflicting and overly complex regulations.

State purchasing agencies have been developing and promulgating their own regulations without paying sufficient attention to other existing relevant regulations or to adequate coordination with other purchasing agencies. This practice over the past ten years has led to volumes of regulations, some of which are confusing, unenforceable, ignored, or in conflict with other regulations.

The result is that provider agencies cannot operate consistently and effectively because of conflicting or complex regulations that are difficult to understand.

Examples

1. The following is one example of a complex regulatory definition:

(a) Excess cost growth shall be the greater of;

(i) zero; and

(ii) The difference between base year adjusted operating costs (computed according to 114.4 CMR 9.10[3]) and the maximum base year reimbursable operating costs (computed according to 114.4 CMR 9.10[b]) below).

(b) Maximum base year reimbursable operating costs shall be the result of the following computation. For the purpose of this subsection the adjective "prior" shall modify the affected noun as if it were followed by the phrase "for the immediately preceding annual review." For example, the prior base year allowed operating costs shall be the base year allowed operating costs which were calculated during the immediately preceding annual review.

A 15-line computation follows the above example as part of the definition.

2. The Office for Children cited one provider because the temperature setting of the provider's hot-water heater was too high and could burn the children. The provider turned the temperature down. A few weeks later, The Department of Public Health cited the provider because the hot-water heater setting was too low to properly sterilize the children's utensils. The provider turned the temperature up. The city health inspectors subsequently cited the provider because the hot-water heater setting was too high and not in conformity with city requirements. The provider was unable to comply with any of the regulations because of the conflicts and ambiguity.

Recommendation

To eliminate conflicting as well as overly complex regulations, EOAF must identify, evaluate, and simplify all existing regulations. EOAF's goal should be the following:

> To the greatest extent possible, simplify all regulations to make them compatible, easily understandable, and accessible without jeopardizing the health, safety, or welfare of those receiving services.

The Executive Office for Administration and Finance (EOAF) must be the central information source for all questions relating to purchase-of-service regulations.

3. Geographical Boundaries

Deficiency

State agencies currently operate independent purchase-of-service programs. Within the Executive Office of Human Services (EOHS), for example, 8 of the 15 agencies operate decentralized field operations divided into as many as 7 regions and 47 areas. Approximately 55 regional and 257 area offices exist, some of which do not share the same geographical boundaries.

Chapter 6A, Section 16, of the Massachusetts General Laws, as amended, states, in part, that the Secretary of Human Services shall establish uniform regional and area boundaries for all agencies within EOHS. Such boundary establishment has not been successfully accomplished. From an organizational and administrative perspective, the current overlapping and conflicting geographical boundaries characterize the general lack of standards and inadequate statewide coordination in the Commonwealth's method of purchasing services.

State purchasing agencies maintaining geographical boundaries that do not correspond with other purchasing agencies' boundaries contribute to the confusion, duplication, and inefficiencies in the present method of purchasing services.

Examples

1. Purchasing agencies within EOHS, such as the Departments of Mental Health (DMH) and Social Services (DSS), maintain separate geographical boundaries for area and regional divisions. For example, a provider that is located in Chelsea and contracts with these two agencies would geographically fall into DMH's Region VI, Area 40, and DSS's Region III, Area 16A. These different geographical boundaries mean that the provider conducts business with two different agency regional/district offices, as well as two different area offices, all having different standards, practices, and procedures. A client seeking services in Chelsea would find the DSS services conveniently located within the city but would have to travel into Boston to the Lindemann Center for the DMH services.

2. Another illustration involves a provider located in West Roxbury. This provider would fall within Region VI for both DMH and DSS but may conduct business with three separate area offices with varying geographical boundaries (see Exhibit 2, p. 21). DSS's Area 36 serves southern Dorchester and West Roxbury/Roslindale neighborhoods, while DMH splits these neighborhoods between two area offices--41 and 36. The provider serving both agencies may be working with two regional offices and three area offices, all with varied policies, standards, and procedures. Dorchester, West Roxbury, and Roslindale clients that both departments serve may find themselves in a maze, because more than one office may be responsible for their services.

Recommendation

The Executive Office of Human Services (EOHS) must develop a redistricting plan whereby all state agencies share common district/regional and area geographical service boundaries. Ideally, whatever geographical terminology is used (region, district, area, service area, health area, catchment area, etc.), the physical boundaries must be standardized.

4. Planning Deficiency

In the past, many agencies have purchased services for which no formal needs assessments were conducted or updated. In some instances, needs assessments were conducted regionally or by area; however, no single statewide standard was used for the needs assessments. While some agencies have begun to conduct formal needs assessments, statewide standards for all purchasing agencies have yet to be promulgated.

As a result, public funds are expended for vacant slots in contract programs. Furthermore, purchasing agencies are unable to determine the location and size of the populations that may require a certain service, and various purchasing agencies may duplicate services.

In 1981, the Commonwealth decided to reserve and fully reimburse (regardless of utilization) work-related day-care services from the private sector. No formal needs assessments were conducted. The contract language provided that "one hundred percent (100%) reimbursement will be guaranteed for all work related slots." The providers invoiced

Exhibit 2
Area Office Variances in Region VI:

Department of Mental Health and
Department of Social Services

DSS Region VI—Area 36

DMH Region VI—Area 36

DMH Region VI—Area 41

the state for all slots reserved. The Comptroller refused to process those invoices for vacant slots, citing his enabling statute, Chapter 7, Section 13, of the Massachusetts General Laws, as amended, which states, in part: "He may require affidavits that articles have been furnished, services rendered and obligations incurred, as claimed." Subsequently, EOAF overruled the Comptroller.

Examples

1. During 1981, one purchasing agency contracted with several providers for services for which the need and total population were unknown. Our audit of 17 of these providers documented that the Commonwealth expended $320,254 for vacant slots, an average of $18,838 for each provider.

2. Another provider we audited was reimbursed $65,740 from December 1979 through March 1982 for a psychiatric treatment program for physically or mentally ill elderly people living in a nursing home. The contractor had not provided services to a single person during these 28 months.

3. An additional seven providers we audited were collectively reimbursed $436,933 even though clients were never served nor services provided.

We have discovered many other instances in which state purchasing agencies have entered into contracts before the need was established.

Recommendations

Before contracting for new services or expanding existing contract services, state purchasing agencies must conduct formal needs assessments according to standards that the Executive Office for Administration and Finance (EOAF) establishes. State purchasing agencies should evaluate certain demographic information, such as population, age, and income level, and consider these statistics when conducting assessments in order to gain as complete an understanding of needs as possible. Finally, the Commonwealth must identify which "core services" it is committed to purchasing and which "core services" it is committed to providing directly. We define "core services" as those services that form such a central part of human services needs that they are essential and given highest priority. As an example, the Commonwealth may commit itself to purchasing all community residential service for the mentally ill and direct-

ly providing institutional services for prison inmates. As part of its effort to improve planning through centralized control, EOAF must determine how often needs assessments must be conducted for all services and on what basis (statewide, regional, area) to do so.

5. Rate Setting Process Deficiency

The combination of varying reporting requirements and poor communication results in a lack of overall coordination in the rate setting process. The Rate Setting Commission's (RSC) enabling legislation states, in part:

> There shall be a rate setting commission, hereinafter called the commission, which shall have the sole responsibility for establishing fair, reasonable and adequate rates to be paid providers of health care services by governmental units, including the division of industrial accidents in the department of labor and industries, and for establishing fair and adequate charges, to be used by state institutions for general health supplies, care, social, rehabilitative or educational services and accommodations, which charges shall be based on the actual costs of each state institution reasonably related, in the circumstances of each institution, to the efficient production of such services in said institution. The commission shall consist of three members appointed by the governor with the advice of the secretary of the executive office of human services.

Currently, the RSC establishes class rates, unit rates for individual providers' contracts and programs, maximum allowable rates, approved budgets for cost reimbursement contracts, class rates with minimum and maximum levels, and rates for individual clients. The RSC has five separate bureaus, three of which are responsible for setting rates for the majority of purchase-of-service providers. Each bureau has its own reporting forms and requirements. Furthermore, no formal system of communication among the bureaus has existed, although more than one bureau sometimes sets rates for a single provider's programs. (We recognize that the Rate Setting Commission is in the process of consolidating the three 07 purchase-of-services bureaus into one bureau.) In addition, the RSC, for the most part, sets individual rates for the programs and/or contracts

that each provider offers, even when the programs or contracts involve the same service. In fiscal year 1982, one bureau set rates for nearly 6,000 provider contracts (including amendments).

The lack of coordination and heavy workload limit the efficiency of the rate setting process. Providers often secure a favorable rate if they are able to package information for and effectively negotiate with purchasing agencies, which forward the negotiated rate to the RSC for approval. The established rate, if too low, may impair the quality of a program. Conversely, if the established rate is too high, the provider realizes surplus income. As a percentage of the maximum contract obligation, this surplus may at times appear negligible. Cumulatively, however, the surplus represents millions of dollars that may be paid in excess of the actual service delivery costs.

Example

One provider we audited had two contracts with a purchasing agency to provide children's services. Two separate bureaus that each set a rate for this provider failed to consider the total of the budgets for the provider's various programs. As a result, the approved rate allowed the provider to be reimbursed at 163% and 150% of the executive director's and business manager's respective salaries.

Recommendations

The Rate Setting Commission's role in the purchase of social and rehabilitative services must be restructured to that of a pricing board. Under this structure, the RSC would set "cost corridors" for all service classes that EOAF approves. (We define "cost corridors" as minimum and maximum amounts to be paid for a unit of service. Standard service classes are service categories, such as mental health, residential care, prerelease, alcohol rehabilitation, day care, and foster care.) The purchasing agency would then be responsible for negotiating a unit rate within the cost corridors that the RSC establishes.

The RSC must establish uniform financial statements, cost reports, and budgets for all providers that contract with the Commonwealth. All financial reporting must be from a total agency perspective, including a detailed account of every program and every contract, including all funding

sources. (Every provider must submit annually a cost report of its operations prior to receiving an approved rate. This reporting requirement should include all day-care center providers that have historically been exempt from filing cost reports.)

6. Integrated Automated Systems

Deficiency

The state's present purchase-of-service method is not sufficiently automated, nor does it ensure integrated systems for data gathering, model assimilation, program and fiscal decision-making and processing. The existing automated systems are dissimilar and incompatible, and they do not address the needs of total purchase of services within the Commonwealth. These systems are agency-specific, with no overall integration. In addition, these systems are not sufficiently protected from unauthorized access.

As noted earlier, purchased services burgeoned during the 1970s. However, the attention necessary to coordinate management, accountability, and planning for automation within the Commonwealth did not accompany this growth. As a result, the Commonwealth's systems currently used in purchasing services are functionally limited, incompatible from agency to agency, and inadequate for planning and management at both the agency and state levels.

The dollar amount of purchased services, the thousands of clients receiving services, and the hundreds of various service categories being purchased require an automated management information system to coordinate statewide management, planning, accountability, and control.

In 1979, the Bureau of Systems Policy and Planning (BSPP) was created to coordinate electronic data processing policy and planning within the Commonwealth. However, not until 1983 did BSPP require state agencies to provide sufficient planning detail for the bureau to develop a statewide data processing plan or to coordinate agency procurement requests.

In an effort to specifically address the lack of coordination among agencies purchasing 07 services, the Executive Office for Administration and Finance (EOAF) in 1983 established the Purchase-of-Service Policy Group (POSPG). The

POSPG is comprised of all state agencies that purchase 07 services, and it is involved in developing an automated management information system that will meet the needs of individual agencies and the Commonwealth as a whole. The State Auditor's Office (SAO) recognizes the establishment of this entity within EOAF as an important first step in improving and formalizing centralized control of purchased services.

Examples

The Commonwealth is unable to determine at any given point in time, through automated systems, the total number of 07 contracts, the total dollar amount of these contracts, the total number of 07 providers, and the total dollar amount by provider. In addition, existing automated systems provide limited assistance in some agency subdivisions and no assistance in most cases for contract administration, including contract monitoring, contract amendment, compliance reporting, quality assurance, cost-effectiveness analysis, client tracking, and vacancy reporting for all purchased services with an agency. As a result, purchased services within the Commonwealth are inadequately managed--lacking information for proper planning, monitoring, and efficiency.

While we found no evidence to support the belief that unauthorized access to these systems has occurred, we believe that the existing and planned systems are inadequately protected. An unauthorized person, for example, may gain access to an automated payment system, process a payment, and delete any record of the transaction.

Recommendations

All purchasing agencies using automated systems must ensure that adequate safeguards exist to prevent unauthorized access. Security is imperative when a remote "call up system" is utilized. BSPP must strictly enforce and adhere to Administrative Bulletin 82-5 (revisions to regulations governing data processing procurement regulations). BSPP must inventory and assess all existing EDP systems currently used (owned or leased) by the Commonwealth. BSPP must develop a statewide data processing plan to ensure that all proposed and future procurements of EDP systems conform to that plan. A joint effort between BSPP and POSPG must be undertaken to indentify the critical issues involved in automating the purchase of services.

A systematized purchase-of-service application must include the automation of all the functions of contract procurement, administration, payment for services rendered, and re-

porting on all agency activities. The system must have the capacity to--

1. Assemble and maintain sufficient provider identification information in a data base;

2. Provide improved control over the departments' budgets and contracts;

3. Strengthen controls and processing efficiency over the departments' encumbrances and expenditures;

4. Assemble financial and operational data that meet all agency reporting needs;

5. Integrate the above four functions and be able to adapt to the agency's internal accounting system for budgeting and expenditure control (This adaptation will reduce the operational expense of keeping the files updated and ensure consistency of data elements in the various subsystem files.);

6. Feature online data entry and inquiry capabilities which permit direct and immediate access to the data base by agency central and regional/area office personnel (Online data entry and inquiry will greatly diminish the paperwork transfer between central and regional/area offices.);

7. Feature a data base management system (DBMS) to improve programming productivity and reduce software development costs (A DBMS will also provide information retrieval capabilities to meet the variety of agencies' needs for information.); and

8. Operate with the Comptroller's budgetary control system with direct input by file posting or magnetic tape transfer. (This feature will further reduce paperwork transfer between agencies and the Comptroller's Office.)

7. Contract Cycle Deficiency

The current method of purchasing services operates on a 12-month cycle that coincides with the fiscal year (July 1 - June 30). All purchase-of-service agreements (AF-7s) technically expire on June 30. Traditionally, purchase-of-service agreements have coincided with the fiscal year to ensure proper budgeting and planning. However, the Common-

wealth's 07 contracts cannot be properly managed under the present purchasing method.

Of the Commonwealth's more than 2,500 purchase-of-service contracts, many are poorly negotiated, rountinely approved without review, and rushed through processing to meet the June 30, 5 P.M. renewal deadline. Frequently, purchasing agencies do not yet know their state appropriation for the upcoming fiscal year, which results in thousands of contracts being renegotiated and amended to reflect the actual appropriation.

Example

One provider had 27 contracts, covering 14 different programs, that 3 state agencies purchased. During the fiscal year 1982 contracting cycle, many of these contracts were hastily negotiated to avoid service disruption on July 1. Subsequently, several contracts were renegotiated and amended when the legislative appropriation did not coincide with the purchasing agencies' budget requests. This practice is costly, wasteful, and inefficient.

Recommendations

The contract cycle must be separate from the fiscal year. This separation can be accomplished by staggering each contract year either by region or by service category (see Exhibit 3, p. 29). For example, Region I 12-month contracts would expire on July 31, Region II 12-month contracts would expire on September 30, etc. Alternatively, separation by service category may have all day-care contracts expire on July 31, all prerelease contracts expire on September 30, etc.

All contracts must contain language similar to the following:

> This contract is subject to appropriation and contingent on the continuing availability of funds.

Adopting these recommendations would--

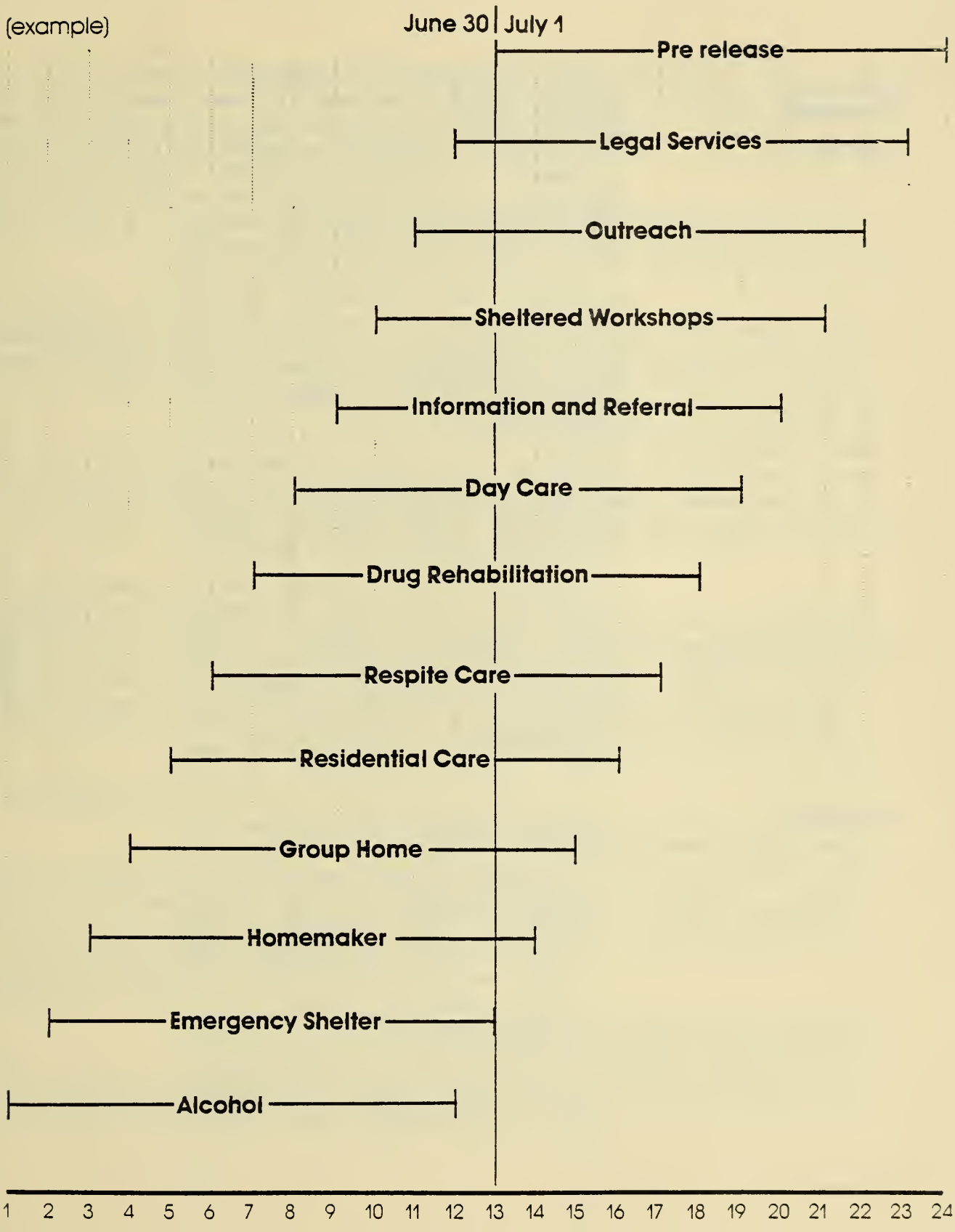
1. Allow for an orderly contract renewal process;

2. Eliminate a weighty administrative process to meet the current June 30 deadline and allow for proper contract negotiation and oversight; and

3. Allow for proper fiscal planning for the service delivery system.

Exhibit 3
Selected Services
Staggered Contact Cycle

12 Month
Contract Cycle



8. Contract Language Deficiency

Contract provisions and requirements vary from one agency to another. Each 07 contract includes general terms and conditions, contract language, and multiple attachments, and the provider is required to submit multiple copies of each document to the purchasing agency. Many contracts do not describe in sufficient detail the service that the purchasing agency has sought to procure. In fact, providers--rather than purchasing agencies--usually prepare contracts.

Inadequate and vague program descriptions result in programs that are different from those that an agency believed it was purchasing. In addition, complex and convoluted contract language may not be readily understood by the provider, resulting in unintentional violation of the contract conditions.

During the past decade, 07 contract language has improved, but each purchasing agency has individually and incrementally changed contract language without coordinating its efforts with those of other agencies.

In addition to uncoordinated changes in contract language, sufficient attention has not been given to program descriptions, services, and goals. Although objectives and outcomes of some social programs are difficult to accurately measure, descriptions in general are often vague and of limited use in evaluating the goals, programs, and cost-effectiveness of different program models for similar services.

Examples

1. The following "Detailed Service Definition" was taken from one contract we reviewed:

> Therapeutic day services to be provided for developmentally delayed "at risk" children 0-3 and their parents . . . . The goal of the program shall be to provide service in the most culturally normative and least restrictive environment possible to maximize their independent functioning within the mainstream of the community.

2. Another contract we audited did not clearly define how a family's second child's fee should be assessed for day care. The following is an excerpt from the contract:

> Fee schedules are based on family income and the cost of care for each program type. Full fee will be collected for the first child from a family in day care, 1/2 fee for the second, and no fee for additional children.

This language is ambiguous and leads to misinterpretation. It does not clearly state whether the second child's fee is 50% of the first child's fee or 50% of the fee for the program that the second child attends.

Recommendations

The Executive Office for Administration and Finance (EOAF) must develop a contract with standard, easily understood language, which all purchasing agencies must use. In addition to the standard contract language, each purchasing agency must attach a detailed statement of the services it is purchasing, as well as a statement of performance standards and measurable, expected results. The contract document must be designed so that relevant information contained in it can be used in an appropriate electronic data processing system (see Recommendation 4, p. 22).

9. Performance Contracts

Deficiency

State purchasing agencies operate independent purchase-of-service programs with varying contractual/noncontractual arrangements. Examples of contract types include cost reimbursement (nonunit), unit, blanket, and purchase agreements. Many of these types of contracts do not contain measurable goals and objectives such as performance standards for program evaluation.

Because of varying contract language and the lack of measurable goals and objectives, purchasing agencies are unable to accurately determine whether they are receiving a quality service at a reasonable and economical price. In addition, state agencies and providers are often confused about what is required or allowable in one contract as opposed to another.

Historically, the state purchased services under cost-reimbursement contracts. This system was seen as an efficient mechanism to start up programs and attract new providers by ensuring that all start-up costs would be reimbursed. More recently, the state has moved toward unit-rate contracts

and purchase agreements. Proponents of the cost-reimbursement method argue that such contracts result in greater provider accountability and budget monitoring. Alternatively, proponents of unit-rate contracts argue that the unit-rate method creates an incentive for the provider to manage resources more efficiently.

In the case of cost-reimbursement contracts, providers have no incentive to be efficient because they will be reimbursed for all costs incurred. Unit-rate contracts provide incentives for efficiency because such contracts often result in the provider generating surplus income when expenses are less than income. Many of these contractual/non-contractual arrangements, however, contain insufficient program descriptions and lack performance measurements.

The lack of standard performance measurements, as well as complicated, duplicative, and voluminous documentation that various contracts require, causes (a) confusion for the provider; (b) inefficiencies by the state and provider; and (c) a general loss of control and accountability in the purchase of services.

Recommendations

The Executive Office for Administration and Finance must require the adoption of a standard, total performance contract system for the majority of services purchased (start-up and phase-down contracts excepted). These contracts must contain definitive performance standards by which the programmatic and financial data will be measured and evaluated. Financial penalties must exist for failing to serve the required number of clients. There should be an opportunity to renegotiate the number of clients served, without penalty, at two points--after five months and after nine months of the contract cycle. If a provider is not within a ten percent margin of serving the number of clients as stated in the contract, it must submit an explanation and a plan of corrective action. At the end of the contract year, the provider must have served 95% of the client population as stated in the contract, or the purchasing agency may proportionately reduce the funding in the subsequent contract year.

To ensure compliance, the contract must state that each provider shall have an annual financial and compliance audit

performed by an independent public accountant. The public accountant will also certify the number of service units by service category and client attendance.

The performance contract should provide for a unit-of-service reimbursement rate. All provider reimbursement requests must be in the form of a standard invoice, which EOAF must develop. Monthly expenditure reports must be submitted to the area office for certification and regional office for approval. Expenditure reports and certification of supporting documentation need not continue beyond the regional office, where they must be kept on file for audit verification. Qualified providers should be reimbursed by means of the Advance Payment System (see Recommendation 13, p. 38).

Performance contracting will facilitate the evaluation process by establishing the goals to be accomplished, the tasks to be performed, and the expected outcomes or results.

10. Multiple Service Contracts

Deficiency

The current method of purchasing services requires multiple contracts between state purchasing agencies and providers that supply a particular service. Many state purchasing agencies, including the Departments of Mental Health, Public Health, Social Services, Elder Affairs, use different geographical boundaries, purchase-of-service standards, reporting requirements, policies, and regulations. Practices often vary within a single agency--area to area and region to region. Each agency, over the past decade, has developed its own requirements and criteria for purchasing services. Consequently, each purchased service has required a separate contract.

The result of multiple contracts is voluminous paperwork and burdensome contract procurement and administrative procedures that vary among agencies.

Example

One provider had 11 separate contracts in one region; the contracts covered 4 programs with 1 purchasing agency. Under the fiscal year 1982 method, the purchasing agency would issue 11 RFPs, and the provider would submit to the purchasing agency 3 copies of each bid, resulting in 33 documents. If all the bids were accepted, the provider would have to produce and submit 77 documents (7 copies each of 11 contracts).

Recommendations

Providers should submit proposals to the regional office for review and selection. Multiple and duplicative contracts between providers and purchasing agencies should be eliminated in favor of a region-by-region, one-budget, single-service agency contract.

Under this system, the provider that, for example, has 11 contracts in one region for 4 programs with 1 agency would have only 4 contracts. Total budgets should identify each separate component of the program and the number of service units and should specify the reporting requirements for each separate component of the program in a given area. Day-to-day supervision and monitoring would remain at the service area level; however, the overall coordination and oversight of contract procurement and administration policy and regulations would be at the regional level.

11. Standard Accounting And Record-Keeping Practices

Of the 1,100 providers that contract with numerous state purchasing agencies, many do not use standard, generally accepted accounting and record-keeping practices.

Deficiency

The numerous state purchasing agencies' varying and conflicting standards, reporting requirements, policies, and regulations have hampered standard accounting and record-keeping practices.

The lack of such practices results in insufficient accountability and control. In some instances, financial records are unauditable. In other instances, providers often submit insufficient and inadequate documentation for expenditures. The lack of standards does not allow for adequate accounting of public funds; often, public funds are commingled with other sources of income.

Example

The General Terms and Conditions section of providers' contracts requires that certain books and records be maintained in accordance with generally accepted accounting principles. During our audits, we cited 18 providers for nonexistent, deficient, or inadequate accounting and record-keeping practices involving funds totalling $15,862,154.

Recommendations

The Executive Office for Administration and Finance (EOAF) must establish standard budgeting, accounting, and record-keeping practices that, as a condition of contracting, all

state purchasing agencies must require providers to adopt. All such practices must be developed in accordance with generally accepted accounting principles. Furthermore, providers must be required to demonstrate basic financial and administrative capabilities in addition to programmatic expertise. Providers must, at a minimum, maintain accurate and timely records with proper expenditure classification ensuring the segregation of public funds. Contract language must specify the types of records required, including those for payrolls, invoices, vouchers, warrants, etc. All providers must, as a condition of contracting, be required to close out or reconcile contract revenue with expenses and submit all required reports in a timely manner. In cooperation with the Comptroller, the Rate Setting Commission, and the purchasing agencies, EOAF should publish all accounting and record-keeping requirements.

12. Client Funds Deficiency

State purchasing agencies do not adequately monitor providers' controls for the safeguarding of, and accounting for, clients' funds.

State regulations (104 CMR 2.13: [10] and 104 CMR 20.06: [3][c]5) provide for the safeguarding of client funds. These regulations state, in part, the following:

> All funds received from the client or on his behalf shall be accounted for and a permanent record made . . . . All funds disbursed shall be accounted for . . . and a permanent record made . . . .
>
> A record shall be kept of every transaction, including the date, amount received or disbursed, the manner in which such funds were managed or expended, identification of involved parties, and receipts for expenditures exceeding $25.

The lack of state agencies' monitoring and the absence of proper controls make client funds vulnerable to abuse.

Examples

1. We audited $2,999 of disbursements from clients' funds that were under the control of one provider agency. Our audit disclosed that $1,151--38%--of these disbursements did not have supporting documentation as required by sound business practices.

2. We audited another provider that established a practice of placing a predetermined amount of cash in an envelope for each client. The provider's policy required that staff make a notation on the envelope whenever money was either disbursed to a client or received by staff to replace expended funds. We tested 15 client envelopes by comparing enclosed cash with amounts listed on the envelopes. In 14 cases, the amounts listed did not agree with enclosed cash.

Recommendations

Purchasing agencies must ensure that provider agencies keep a permanent record by which to account for all funds received on behalf of the client and disbursed to the client. Provider agencies, as a condition of recontracting, must demonstrate adequate systems for safekeeping of client funds. In addition, the annual financial, compliance, and performance audit, performed by an independent public accountant, must include a review of the recording and accounting of client funds.

13. Interest Payments and Untimely Reimbursements

Deficiency

Provider agencies assert that they experience cash flow problems due to the costs associated with program start-up and untimely fiscal year-end state payments. Consequently, many providers borrow funds at high interest rates from commercial lending institutions.

These borrowing practices result in substantial additional cost to the Commonwealth, since providers are often able to recapture the interest payments from the state by building this allowable cost into their operating expenses. It is estimated that in fiscal year 1980, the cost for interest repayment exceeding the actual cost of service provision was $4.7 million dollars.[3]

The Commonwealth is prohibited from advancing public funds to provider agencies. When provider agencies incur costs to start new programs (for example, to purchase a building for a community residence program), the state cannot provide up-front capital assistance. Providers are forced to borrow from private sources. Similarly, at the end of the

[3] Massachusetts Council of Human Service Providers, A Survey of Financial Management Problems Among Human Service Providers in Massachusetts (Boston, 1981).

fiscal year when the Comptroller is closing old and establishing new accounts and the legislature is in the processs of passing a new fiscal year appropriation bill, providers may wait as long as five months (July through November) for state reimbursements. Providers' cash flow problems necessitate borrowing.

In addition to costs associated with program start-up and fiscal year-end delays, a number of invoicing problems can cause the state to delay payments to providers. For example, if the provider improperly fills out an invoice or an unauthorized person signs it, the invoice will be rejected, and the provider will not be reimbursed. Similarly, if the required back-up documentation is not legible, payment will not be rendered. These infractions result in the entire invoice being rejected and returned for resubmittal. Subsequently, the invoice must be reexamined and approved.

In an effort to respond to invoicing delays inherent in the Regular Payment System (see Glossary), the Commonwealth instituted a Timely Payment System (see Glossary), which the Comptroller later revised to the Advance Payment System.

This system made payment processing possible on an average of 14 days. Subsequently, other purchasing agencies instituted their own payment systems that followed the Return of Advance process. At the four purchasing agencies we audited, only 20% of the payments to providers were processed through the Regular Payment System.

The present Advance Payment System sufficiently addresses the timeliness of processing payments to those providers that have demonstrated sound bookkeeping and invoicing practices. Costs to providers and to the Commonwealth associated with capital financing of new programs and fiscal year-end delays remain to be addressed. Streamlining the contract cycle (see Recommendation 7, p. 28) and eliminating cost-reimbursement contracts (see Recommendation 9, p. 32) should adequately reduce these start-up and fiscal year-end costs.

xamples

1. Of the providers sampled in a recent survey, 46% experienced average estimated borrowing costs of almost $6,400 each in fiscal year 1981.[4]

[4] Ibid.

The interest rate charged to providers averaged 13.9% when the survey was conducted. Nearly 75% of provider agencies surveyed reported serious cash flow problems.[5]

2. Our audit of one provider agency revealed that the provider incurred interest expense of $2,219 on a three-month, fiscal year-end loan that DMH reimbursed. In fiscal year 1981, this provider earned $2,848 in interest income. The provider did not offset the interest expense against the interest income. Had such an adjustment been made, the state would not have reimbursed the provider for the interest expense.

Recommendations

The present Regular Payment System should apply only to those providers that do not use sound bookkeeping and invoicing practices. To alleviate fiscal year-end delays and to decrease the volume of the accounts payable for prior fiscal year invoices, providers should be encouraged to submit invoices weekly, beginning the first week in May.

When providers have demonstrated sound bookkeeping and invoicing practices, they should be allowed to participate in the Advance Payment System, subject to the Comptroller's approval. Particular attention must be given to the accuracy of the invoice and the supporting documentation. In addition, the Comptroller must analyze the controls and edits used in the Advance Payment System to ensure that the proper safeguards are in place to avoid duplicating or overpaying invoices. Interest expense, as an allowable cost that will be reimbursed by the state, must be limited to net interest expense only. Purchasing agencies must ensure that providers offset any interest expense against interest income. In addition, the Rate Setting Commission must establish a ceiling for annual net interest expense which will be reimbursed by the Commonwealth.

Finally, the Comptroller should consider the feasibility of extending the Departments of Public Welfare's and Social Services' Advance/Accounts Payable System to all state purchasing agencies.

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[5] Ibid.

14. Reimbursement For Vacant Contract Slots

Deficiency

As a result of past contract policy, the Commonwealth reimburses providers for empty or vacant slots or beds. Various approved absence policies allow a provider to be reimbursed at 100% of the capacity that the Commonwealth has determined, even if, for example, the provider's program operates at 80% or 85% of that capacity.

Because of this policy, the Commonwealth has expended public funds for services that were never rendered.

The level of vacancies corresponds, in part, to the type of referral system used for a given program. Two types of referral systems exist for purchased services: first, the closed referral system (in which the state is the sole purchaser and refers all clients); and, second, the open referral system (in which the state is one of many purchasers and may procure less than 100% of the provider's services). Under both referral systems, the Commonwealth reimburses providers for excessive vacancies if the client population is not accurately assessed or if the provider fails to enroll 100% of capacity.

Examples

1. Our audits revealed that one purchasing agency reimbursed 13 providers a total of $263,711 for vacant slots.

2. One provider we audited held a fiscal year 1982 contract totalling $78,287 for a purchased service with the state. During October, November, and December 1981, the purchasing agency reimbursed the provider $17,982 for vacant slots. The actual enrollment was only 22% of the program's capacity, and the actual attendance was only 18%. The provider was reimbursed for 100% of the capacity.

3. During our audits, we cited 17 providers (including the provider in Example 2) for receiving reimbursement from state agencies for vacant beds or slots when, in fact, the services were never provided. These inappropriate billings and reimbursements totalled $320,254. The 17 providers had 59 contracts, representing 5% of the Commonwealth's total purchase-of-service contracts. However, the inappropriate reimbursements could total in the millions of dollars statewide.

Recommendations

The Commonwealth must adopt a uniform vacant bed/slot policy. To do so, the Executive Office for Administration and Finance (EOAF) must--

1. Establish a time limit on long-term vacant bed/slot payments;

2. Develop a uniform, consistent short-term vacancy policy; and

3. Develop guidelines for paying start-up and phase-down costs to ensure that all payments are reasonable and justified.

The vacant bed/slot policy must be applied to both types of referral systems. In a closed referral system, the purchasing agency must develop a timely referral mechanism to ensure that vacant beds or slots are at a minimum at any given time. In an open referral system, the provider must bear the burden of expenses associated with vacancies. If the state is contracting for 60% of the slots, then the state should reimburse the provider for the allowable costs associated with no more than 60% of the program.

In addition, EOAF must establish policies governing reimbursement for vacancies due to special situtations such as program start-up and phase-down. Such policies should include specific time limits after which the Commonwealth will not reimburse providers for vacant beds or slots.

15. Surplus Income Deficiency

The current method of purchasing services does not ensure that the state is paying only for the cost of those services actually rendered. Providers are not required to match revenues with expenses before final invoices are submitted.

Provider agencies are realizing surplus income. In most cases, such surplus income is the result of revenue from unit-rate contracts. The unit rate is calculated from a budget of estimated costs that the provider submits to the Rate Setting Commission (RSC). If the provider agency delivers the unit of service at a lower cost than projected, it realizes a surplus when it receives payments

from the state purchasing agency. Certain costs associated with heat, light, power, rent, insurance, personnel, fringe benefits, and administration, for example, are usually estimated in the original budget and are therefore reflected in the rate at which the provider will be paid. When the actual cost of these items is documented, it is often less than what was budgeted. As a percentage of the maximum obligation of each contract, this surplus appears negligible. Collectively, however, the surplus represents substantial public monies paid out in excess of the actual costs incurred in delivering the services.

Examples

1. During our audits, we cited 11 providers that realized a total of $395,197 in surplus income. If this sample is representative of the entire 07 provider population, the providers may have realized more than $35 million in surplus income during fiscal year 1982.

2. Our review disclosed one provider that, as of June 30, 1982, had accumulated $5,540 in surplus income. Of this total, $4,683 resulted from a 1976 Department of Public Health (DPH) Division of Alcoholism overpayment on a $10,400 contract. The provider reported the surplus (which equaled 46% of the total contract) to DPH in June 1976. As of September 1983, DPH had not taken action to recoup the overpayment.

3. One provider we audited had fiscal year 1981 contracts totalling $128,914 with the state and realized a surplus of $17,369 during that fiscal year. Furthermore, during the past seven years, the provider has accumulated approximately $150,000 in surplus income from the state.

4. According to one purchasing agency's estimates provided to our auditors, in fiscal year 1983, the purchasing agency made a total of $427,357 (from a total budget of $22.9 million) in overpayments in one service category. Furthermore, the aggregate amount of outstanding overpayments that the agency made (current year plus prior year amounts not collected) was $788,302 at the close of fiscal year 1983 for that single program that the agency purchased.

Recommendations

Before the final invoicing and payment, all purchase-of-service agreements must have actual allowable costs recon-

ciled with actual service delivery costs. Furthermore, contract language must provide for monetary adjustments in subsequent contracts and recovery of surplus income. Such language could state:

> Both parties agree that the state has the right to recover or deduct funds from this contract or future contracts based on discovery of facts of confirmed overpayment or improper use of funds.

In addition, EOAF must ensure that procedures are developed to detail the method by which the Commonwealth should recover surplus funds from providers.

16. Real Property Deficiency

Controls and oversight mechanisms are inadequate to ensure that the Commonwealth is not excessively reimbursing providers for the principal and interest costs of mortgages on properties that the related parties purchase.

The lack of standards and of proper contract procurement and administration practices has resulted in the Commonwealth's reimbursing providers (or related parties) for mortgage costs (principal and interest) that the related parties incur in purchasing property. The Commonwealth does not retain any equity in the property and often reimburses providers at a rate that will pay off the mortgage in less than six years.

Article XLVI, as amended, of the Articles of Amendment to the Commonwealth's Constitution (the "Anti-Aid" Amendment) prohibits the use of public funds for the aiding or maintaining of hospital, institution, school, charitable, or religious undertakings in facilities that are not publicly owned and under the Commonwealth's or its authorized agent's exclusive control. As a result, many providers have created separate legal entities known as "real estate trusts" or "holding corporations," which purchase the assets, and, in turn, rent them back to the provider.

Example

During our audit of one nonprofit provider, we noted that the nonprofit corporation was rendering services in a residence rented from a realty trust corporation. The principals of both corporations were the same individuals. The

purchasing agency was reimbursing the provider for rental expenses at double the monthly rate of the mortgage payments that the realty trust made. If the contract continues to provide for the same rental rate, the mortgage would be retired in five years. The realty trust may then accumulate substantial profits if it continues to charge rent to the provider that the state purchasing agency is reimbursing. If the provider chooses to no longer contract with the purchasing agency, the Commonwealth would hold no equity in the residence that public funds paid for. In addition, the clients may have to be relocated to another facility.

Recommendation

The purchasing agency, during contract negotiations, and the Rate Setting Commission, while establishing cost corridors, must ensure that a provider's cost report distributes the principal and interest costs of the mortgage over a reasonable number of years (such as 20 years). The Rate Setting Commission shall establish the standard for what is to be considered a "reasonable" number of years.

In addition, the purchasing agency and the Rate Setting Commission must ensure that the rental payments do not exceed the fair market value of the property on an annualized basis.

Contracts providing for rental payments which have historically exceeded fair market value must be reviewed by the purchasing agency and Rate Setting Commission. Should these contracts be renewed for future fiscal years, language should be included in the contracts that, if the provider should fail, allows the Commonwealth to place a lien on the property equivalent to the excess rental payments.

Finally, the Commonwealth must clarify the "Anti-Aid" Amendment (Article XLVI, as amended), including defining what constitutes a public purpose as applied to 07 contracts.

17. Purchase and Inventory of Furniture and Equipment

The process by which providers contracting with state agencies purchased furniture and equipment with public funds inadequate and did not allow for accountability.

Deficiency

As a result, furniture and equipment purchased with public funds often cannot be identified or located.

In the past, the Commonwealth included a furniture and equipment line item in the contract budget so that the provider could purchase materials necessary to operate its program. While some purchase-of-service agreements require that purchasing agencies maintain an inventory of such items, purchasing agencies and providers have often ignored this requirement. In 1982, the state's Purchasing Agent prohibited the continuation of furniture and equipment being purchased from the 07 subsidiary account.

The purchasing agency must now requisition, under the 15 subsidiary account (furniture and equipment), all furniture and equipment. Such requisitions must be processed through the state Purchasing Agent's Division.

Examples

1. We noted deficient furniture and equipment purchasing practices during our audit of a provider that purchased $13,000 worth of custom-made desks, beds, and bureaus. While this furniture was specially designed for the clients, it had been stored in a warehouse for two years because it would not fit into the clients' rooms. Some of this furniture was subsequently cut up to construct playground equipment for the clients.

2. We audited one provider that had purchased $30,000 worth of furniture and equipment yet was reimbursed $31,056. Of this furniture and equipment, 75% had been stored in a basement for 18 months. At the time of our audit, warranties applicable to the major appliances had expired, because 17 months had passed since the provider purchased the furniture and equipment.

3. Another provider we audited could not locate washing machines, dryers, and stereos valued at a total of $2,099.

Recommendation

Title to furniture and equipment purchased with public funds should be held by the purchasing agency. Purchasing agencies must require that all providers immediately inventory all furniture and equipment purchased with public funds. Such inventory must include not only the description of the item but also the cost, physical location, and use of the item. A master file of this inventory must be computerized and kept on file at the purchasing agency's

central office and at the Executive Office for Administration and Finance (EOAF). In addition, all furniture and equipment inventories must be updated annually. Furthermore, EOAF should provide for unused or underused furniture and equipment to be allocated to the purchasing agencies.

Before a purchasing agency requisitions new furniture or equipment, it must verify that surplus or underused items do not exist elsewhere in the system.

18. Client Records

Deficiency

Contract conditions that most purchasing agencies use allow providers rather than the agencies to retain the right to client information and client records when the contract is terminated.

The result of this provider right is that the state forfeits client information and records, loses substantial control over the future treatment of clients, and is less able to plan and account for their service needs.

Because many recipients of state-funded, but privately provided, services have a history of involvement with state human service agencies, loss of client records each time a recipient leaves a program is inefficient and illogical. When providers retain client information upon contract termination, recordkeeping is duplicated and, more importantly, clients may not continue to receive needed services.

Example

During the past few years, a number of providers have stopped contracting with the Commonwealth. If a provider's records, including valuable client data, are not available to a subsequent provider agency that assumes control of a program, the time-consuming and redundant task of re-creating client and program data would have to be undertaken.

Recommendation

Language must be included in all 07 contracts requiring that client records be turned over to the purchasing agency when programs and contracts with provider agencies are terminated. An example of such language may be:

> When the contract is terminated, all finished or unfinished documents, data, studies and reports, including clients' records and reports,

that the corporation prepares, shall become the department's property in accordance with this agreement.

19. Precontract Provider Qualifications

Deficiency

No formal, statewide, precontract qualifications exist for providers that bid on social and rehabilitative services.

The absence of precontract qualifications often results in inadequate service delivery, violations of regulations and contract requirements, and multiple contract amendments. Purchasing agencies contribute to this problem by failing to systematically evaluate the ability of the prospective providers to perform anticipated services. In some instances, providers do not adequately demonstrate programmatic capabilities, but are reimbursed by purchasing agencies even when serious programmatic deficiencies exist. In other cases, providers maintain inadequate financial records that may or may not reflect their financial condition.

The problems of providers with inadequate financial capabilities and/or inadequate service provision were prevalent during the early and mid 1970s. More recently, however, incidences of providers filing for bankruptcy, failing to keep adequate financial records, and having serious programmatic deficiencies are occurring. For example, since March 28, 1983, the State Auditor's Office has been attempting, without success, to audit one provider agency. The agency's director did not attend a scheduled entrance conference and also refused to provide us with its financial and program books and records relating to its purchase-of-service contracts with the Commonwealth. Our site visits in April 1983 to the provider's office and its service center revealed that the locations were apparently vacant. The provider began contracting with the Department of Public Welfare (DPW) in 1977 and with the Department of Social Services (DSS) in 1980. In August 1982, following an area office investigation of the provider's failure to deliver services as specified in its contracts, DSS terminated all contracts with this provider. The provider was both programmatically and financially deficient, yet was not screened out as such at the beginning of the contract cycle.

Examples

1. The most dramatic example of deficient financial record-keeping is a provider with fiscal year 1982 DSS contracts totalling more than $303,000 that, at the time of our audit, maintained receipts of paid bills by putting the receipts in cardboard boxes or in a drawer of an end table. This provider also threw out classroom attendance sheets, which are the original documentation for verification of filled slots.

2. Programmatic deficiencies exist in the form of inadequately maintained facilities. One provider delivered services from a poorly kept facility that had a littered front yard and a malodorous, poorly lit, and unsanitary interior.

3. The Commonwealth reimbursed one provider $65,740 over a three-year period for a psychiatric treatment program that never served any clients. The program was designed for physically or mentally ill elderly patients.

4. Our audit revealed a total of 18 providers that maintained nonexistent, deficient, or inadequate accounts and records for contracts totalling $15,862,154. In addition, we cited 4 providers for delinquent payment of federal and state taxes totalling more than $100,000. Furthermore, 6 providers were violating the public charities' financial reporting requirements.

Recommendations

EOAF must develop precontract criteria. These criteria must require that the prospective provider be able to programmatically and financially provide the anticipated services before the provider is eligible to enter into state contracts. Such criteria must ensure that providers meet all legal and regulatory requirements, complete financial statements, and implement proper accounting systems. In addition, programmatic criteria, including staffing plans and cleanliness and appropriateness of the program space and location, must be developed. These requirements must be included in the request for proposal. Furthermore, prospective and renewed providers must sign an affidavit of compliance, under the penalty of perjury, that all standards and filing requirements (financial, public charity, tax, etc.) have been met or, in the case of a new provider, will be met.

If it is discovered, in an audit or by other means, that a provider has not complied with the standards and criteria,

the purchasing agency must seek administrative and/or financial recourse (see Recommendation 23, p. 53).

20. Conflict of Interest

Deficiency

Purchase-of-service agreements between state agencies and providers are not properly monitored to prevent potential conflict-of-interest situations. Chapter 268A of the Massachusetts General Laws, as amended, provides for the conduct of state employees regarding additional compensation, offers, and gifts.

The general terms and conditions of most purchase-of-service contracts prohibit a provider from knowingly employing, compensating, or arranging to compensate any state employee in violation of Chapter 268A of the Massachusetts General Laws, as amended.

Due to material weaknesses in internal controls on the part of some providers and various purchasing agencies, a significant number of potential conflict-of-interest situations have been discovered.

Examples

1. During our audits, we identified 121 individuals who appeared on both the Commonwealth's personnel records and provider agencies' records.

2. Our audit of one provider agency revealed its hiring of a "program development specialist" who actually functioned in the capacity of junior accountant at the purchasing agency's area office. Part of this employee's responsibilities included reviewing materials submitted by, or relevant to, the provider that "employed" this individual.

3. During the course of our audits we discovered one individual who was a full-time state employee and who was also listed as a consultant on four separate providers' records.

Recommendations

All purchase-of-service agreements must prohibit a provider from knowingly employing, compensating, or arranging to compensate any employee in violation of Chapter 268A of the Massachusetts General Laws, as amended.

Additionally, all purchasing agencies must identify all potential conflict-of-interest situations and notify appropri-

ate providers and affected employees. Employees and providers who have been advised of possible violations of Chapter 268A must request a formal written opinion from the State Ethics Commission. Any employee or provider who fails to request such an opinion within 30 days of notification shall have their contracts or employment with the Commonwealth suspended by the purchasing agency (or agencies) until a formal opinion is rendered. The purchasing agency shall subsequently notify the appropriate office(s), such as Attorney General, Ethics Commission, etc., of the potential violations.

21. Training for Contract Personnel

Deficiency

The Commonwealth has provided inadequate training in contract negotiation and administration and financial management to area and regional office staff involved in contract procurement and administration. While some purchasing agencies are presently providing training, no formal statewide training programs for procuring and administering contracts or qualifications for state personnel exist.

Area and regional staff often lack adequate training in contract procurement, negotiation, and administration. Most of these are unique to a specific agency and are sometimes in conflict with those of another agency. Often policy and practices vary from region to region and from area to area within the same purchasing agency. During our review of state purchasing agencies, certain contract procurement and administration personnel reported that they had participated in general training sessions on the contract manual and the rate setting budget forms, but most expressed a need for more specific training in financial management and contract negotiation.

Examples

1. One provider we audited was reimbursed $245,590 for fiscal years 1981 and 1982 for providing residential psychiatric services. The provider, however, did not render the residential psychiatric services stated in the contract. Instead, the provider charged $4,500 a month against the contract for salaries of employees caring for three potential residential clients who were living in staffed apartments maintained by rental payments that a different contract funded.

2. We audited one provider who received from a state institution a client that had infectious hepatitis. Because of inadequate health-screening procedures and training of state personnel, the provider was unaware of precautionary measures that should have been taken to protect other clients and staff from being infected. Two staff members were infected before the contagious nature of the hepatitis was discovered.

Recommendations

Regional and area state personnel participating in contract procurement, negotiation, and administration must receive appropriate training and certification. The Executive Office for Administration and Finance (EOAF), in cooperation with purchasing agencies' central offices, must develop a curriculum to address these issues.

In addition to training, each purchasing agency should establish a multidisciplinary contract team in each region. This team must be comprised of personnel with budgeting, program, negotiating, and accounting expertise. This team will coordinate each program contract (see Recommendation 10, p. 34) and assist in any contract procurement or administration issue that requires its attention.

22. Contract Monitoring Deficiency

Because regional and area offices of state purchasing agencies insufficiently and inadequately monitor contracts, providers' compliance with fiscal and programmatic contract provisions is not ensured.

The close philosophical and actual working relationships between the state social and rehabilitative agencies' area and regional offices and the providers make it difficult for those offices to independently evaluate and monitor provider performance. Many staff members of state social and rehabilitative agencies share providers' genuine concern for, and advocacy of, client well-being and service delivery. Attempts to ensure accountability, however, generally result only in duplicated paperwork. Area, regional, and central offices--in addition to executive offices, the RSC, and the Comptroller--frequently approve the same documents for technical accuracy, while little attention is subsequently given to qualitative and quantitative aspects of provider performance and contract administration.

The result of inadequate contract monitoring is that the Commonwealth cannot guarantee that all services for which it has paid were ever fully delivered or that program quality and cost-effectiveness of purchased services are at the highest possible levels. Furthermore, when limited financial resources are available and the expenditure of public monies is not closely monitored, the Commonwealth's most needy citizens are not assured of receiving services and treatment that the state is committed to providing.

Examples

1. We audited one provider whose financial statements classified a $12,213 entry as "due the Commonwealth." The purchasing agency's area office was unaware of the overpayments until the provider notified the office. The provider inquired as to how it could return the $12,213 to the state. The area office responded that it (the purchasing agency) was unaware of any mechanism for reimbursing the Commonwealth, although such mechanisms exist.

2. Our audit of one provider agency disclosed the fact that state contract funds were not being used as intended for clients or programs. The provider agency in question issued two low-interest loans totalling $10,500 to its two codirectors for their personal use. The loans were made from an account containing state funds that the state purchasing agency provided for program services.

3. One provider we audited transferred $66,000 in public funds to a former principal who was residing out of state. Furthermore, the same provider transferred $35,000 in public funds to an out-of-state bank without explanation or approval.

4. Another provider we audited inappropriately used public funds to provide certain bonuses, such as hams or turkeys, to 51 employees.

Recommendations

State agency personnel must be held accountable for monitoring and evaluating providers' compliance with contract conditions, and the central office must review the personnel at regular intervals to ensure satisfactory performance of monitoring functions. Specific emphasis by state agency monitoring personnel must be placed equally on fiscal and programmatic quality assurance. Area and regional office

personnel's repeated failure to adequately monitor the purchase-of-service contracts should result in corrective or disciplinary action for state personnel, including suspension, transfer, or termination.

Changes in budgets or contract-supported activities must receive written approval before such changes are made. The provider's failure to obtain prior written approval of amendments must result in the agency disallowing such costs.

The provider must submit for all contracts and noncontractual agreements a monthly expenditure and program performance report to the area office for certification and to the regional office for approval. Submission of the required reports does not necessarily fulfill the contractee's responsibility. Such reports must also meet the content requirements specified in the contract terms. Failure to submit the required reports within the allowable time will result in withholding of payments, withholding of additional awards for the project, suspension or termination of an active contract, or other enforcement action (see Recommendation 23, p. 53).

Furthermore, area and regional offices must maintain current contract files that contain, at a minimum for each contract, the following:

1. A signed contract (including the budget);

2. RFP and bidder's response;

3. Documentation of the negotiation process; and

4. Copies of all required financial and program performance reports from the provider.

23. Contract Enforcement

Deficiency

Purchasing agencies currently have insufficient and inadequate policies and mechanisms for enforcing laws, regulations, and contract conditions pertaining to providers' fulfillment of contract provisions and delivery of contract services.

As a result of these policies, purchasing agencies continue to contract with programmatically and/or financially deficient providers that the agencies know, or should have known, are not complying with the contract terms. Purchasing agencies are generally reluctant to impose any sanctions on deficient providers, asserting that new providers often are unavailable to service clients.

Currently, contract enforcement and recovery of misspent public monies are accomplished primarily through the cooperation and intervention of the Department of the Attorney General, rather than through actions by appropriate purchasing agencies.

Examples

1. One provider we audited had contracted with a purchasing agency for five years. During fiscal year 1982, the provider had contracts exceeding $400,000 with the agency. The provider's accounting records consisted only of a checkbook. Furthermore, the provider was violating the public charities' reporting requirements, had never had an independent audit performed as required, and had not complied with the Rate Setting Commission's request to file a cost report.

2. Our audit of another provider that has received more than a total of $7.4 million from federal, state, and private sources in the last five fiscal years revealed that no total-agency audits were performed annually. The provider's financial statements were not prepared in accordance with generally accepted accounting principles. In addition, the provider violated general contract conditions by failing to file audited financial statements for fiscal year 1982 with the Attorney General's Public Charities Division.

3. Our audits revealed six providers who did not maintain adequate records of clients' financial eligibility to receive services. We sampled 162 files and discovered that 80 files--49% of the total--contained insufficient documentation.

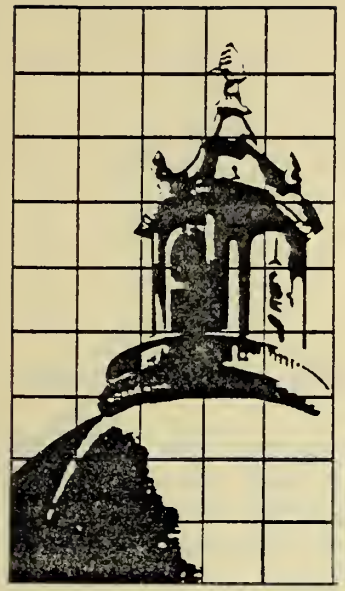
Recommendations

The Commonwealth must adopt administrative procedures, laws, or regulations that address suspending and terminating provider contracts, excluding providers from contracting with the Commonwealth, and withholding funds from providers when programmatic, financial, or compliance deficiencies exist.

Purchasing agencies should withhold funds if a provider has failed to make satisfactory progress in correcting any deficiencies. Furthermore, if the provider has failed to provide adequate accounting of funds, the purchasing agency should not continue to contract with the provider beyond the current budget period. If the deficiency is serious enough, the contract should be terminated immediately.

EOAF must exclude provider organizations from eligibility to receive state contracts under certain conditions, including criminal actions and/or fiscal abuses by provider personnel responsible for public funds.

In addition, Chapter 93, Section 9B, and Chapter 266, Section 67B, of the Massachusetts General Laws, as amended, should be cited in all purchase-of-service agreements. (These chapters are the civil and criminal statutes that provide for fines and imprisonment for submitting false, fictitious, or fraudulent claims to the Commonwealth.)



Chapter V
Conclusion

The Blueprint for Reform presents 23 selected financial and management deficiencies which have been highlighted during our audits of provider agencies and reviews of state agencies. These deficiencies are a direct result of the lack of planning, standards, accountability, control, and efficiency by the Commonwealth in the purchase of services. The Blueprint for Reform not only documents these deficiencies but also presents specific recommendations, principles, and practices which, when implemented, will improve what has come to be a vast, complex, and costly purchase-of-service method.

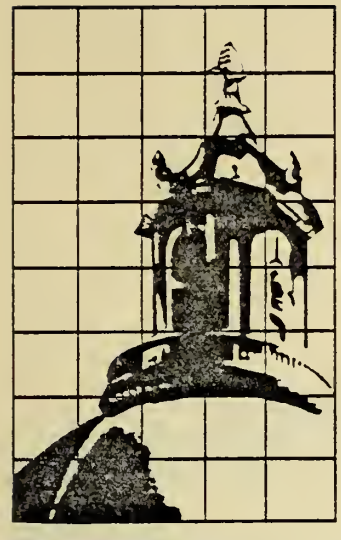
The Blueprint for Reform does not address every weakness in the present purchase-of-service method. Rather, it focuses on components that the State Auditor's Office (SAO) believes to be the major deficiencies. Each recommendation presented in this report is one mode of correcting a documented weakness. We recognize that there may be other options.

Since the Commonwealth of Massachusetts will continue to expend public funds to purchase social and rehabilitative services from the private sector, the contract procurement and administration functions must be substantially improved. The State Auditor's Office firmly believes that such improvements will begin when the Commonwealth adopts and implements the recommendations contained in the Blueprint for Reform. As part of its commitment to creating an improved purchase-of-service system, the State Auditor's Office will establish an "institute" for the certification of public and private auditees and financial managers. The "Auditor's Institute" will offer regularly scheduled programs covering such areas as:

- The SAO's auditing policies and practices;
- Governmental auditing standards for the auditing of accounts, books, and records of all departments, offices, commissions, and activities of the Commonwealth;
- Governmental auditing standards for the auditing of provider agencies; and

- Generally accepted accounting and bookkeeping practices.

Participants' successful completion of any of the above programs will result in certification that they possess adequate comprehension of auditing, accounting, and contracting principles. In accordance with Chapter 11, Section 12, of the Massachusetts General Laws, as amended, the Auditor of the Commonwealth will continue to conduct audits of providers and reviews of state purchasing agencies to monitor the Commonwealth's progress in introducing sound management practices into a multimillion dollar purchase-of-service enterprise.



Chapter VI
Glossary

07 Regulations — Rules governing the purchase of social and rehabilitative services from a nonstate entity, as set forth in the Code of Massachusetts Regulations 801.25 et seq.

Advance Payment System — A payment mechanism that an agency, with advances drawn from the state treasury, administers. Ordinarily, payment is received by the provider two weeks after the invoice is submitted.

AF-7 — An Executive Office for Administration and Finance form used to approve a purchase-of-service plan; details contract-specific information including type of service, service units, duration of contract, rate, etc.

AF-7A — An Executive Office for Administration and Finance-approved form that is used to amend the AF-7.

Anti-Aid Amendment — Article XLVI to the Massachusetts Constitution stating that public money may not be used to aid individuals, private associations, or privately owned corporations.

Audit — A term used to describe not only accountants' and auditors' work in examining financial statements, but also their work in reviewing for (1) compliance with applicable laws and regulations, (2) economy and efficiency of operations, and (3) effectiveness in achieving program results.

Bidder — The party that submits a proposal for services to a state agency in response to a request for proposal.

Blanket Contract — An approved contract that governs the purchase of a service. The total amount spent on the contract is governed by control over use rather than by a stated maximum obligation for each contract.

Closed Referral System — The state is the sole purchaser of a particular service and refers all clients to a designated provider.

Consent Decree — A settlement arrived at by the opposing parties to a legal suit. With the judge's endorsement, the settlement becomes binding. (A prominent example of a consent decree occurred

	in the early 1970s when the parents of students at the state's schools for the mentally retarded brought suit against the state to improve conditions at the schools.)
Contract	A legally enforceable agreement for a provider to render services for which it will be paid by the Commonwealth. Such an agreement is executed in the Commonwealth's name by one of its agencies.
Contract Officers	State agency personnel charged with monitoring and administering social and rehabilitative service contracts.
Control	A term related to management that involves a continuous cycle of monitoring, evaluation, planning, implementation, and measurement.
Core Services	Services that have been designated to form such a central part of the social and rehabilitative services needs that they are essential and given highest priority.
Cost Corridors	Parameters that establish a minimum and maximum amount to be paid for a unit of service.
Cost Reimbursement Contract	A nonunit contract, based on the program budget that reimburses all costs associated with a program. Payment is made based on documentation of expenses, not on service provision.
DEA	Department of Elder Affairs.
Decentralization	The distribution of the administrative functions of a central authority among field or local authorities.
Deinstitutionalization	A policy decision that, in Massachusetts, began in the 1970s and enabled mental health clients to receive active treatment in community settings rather than in state institutions.
DMH	Department of Mental Health.
DSS	Department of Social Services.
DYS	Department of Youth Services.

EOAF	Executive Office for Administration and Finance.
EOHS	Executive Office of Human Services.
Evaluation	An examination of the purchased program against predetermined program performance standards and outcome measurements.
Fiscal Conduit	A private corporation that provides accounting and contract billing services to a purchasing agency for purchase-of-service contracts.
Fiscal Year	The 12-month period beginning July 1 and ending June 30.
Invoice	A document that a provider submits for reimbursement of allowable expenditures incurred in providing services under a purchase-of-service agreement.
Monitoring	A process using management-specific tools to ensure compliance with the terms and conditions of a purchase-of-service contract, as well as to measure performance according to program specifications.
Needs Assessment	The process of establishing the extent of the need for services among the population to be served. The assessment includes review of items such as resources for service delivery, use of current resources, types of services provided, and geographical distribution of resources.
Open Referral System	The state is one of many procurers and purchases less than 100% of the provider's services under a particular contract.
Performance Contracts	Service provision contracts that identify and define certain factors that will be utilized to evaluate a provider's programmatic and financial performance.
Phase-Down Contract	A contract designed to allow for state reimbursement to providers for only those costs associated with closing out an existing program.
Procurement	The process of purchasing services from the private sector.
Provider	The party that contracts with or has an economic relationship with the Commonwealth to provide services such as day care, home care, mental health, or rehabilitation.

Purchase-of-Service System — A purchased, community-based social services system, as opposed to direct service provision by a state agency.

Rate — The amount of compensation calculated by per unit of service (e.g., hour, visit) or fixed by maximum obligation, as established by the Rate Setting Commission.

Rate Setting Commission — Established by Chapter 6A, Section 32, of Massachusetts General Laws, the Commission is an agency placed by statute in the Executive Office of Human Services, which has the sole responsibility for establishing fair, reasonable, and adequate rates to be paid to providers entering into purchase-of-service contracts with the Commonwealth.

Return of Advance — The process of reconciliation of all advanced funds received from the state treasury by the purchasing agency and forwarded to the Comptroller for accounting purposes.

RSC-600 — A Rate Setting Commission form that documents historical costs for programs. Providers complete the form and submit it directly to the Commission.

RSC-600B — A Rate Setting Commission form that budgets future costs for individual programs and contracts.

Rollover Contract — A contract which is renewed on an annual basis, as provided in 801 CMR: 25.07(12).

Sliding Fee — A monetary fee that service recipients pay and that varies according to the services received or the ability of the individual to pay.

Start-Up Contract — A contract designed to allow for state reimbursement to providers for costs associated with establishing a new program.

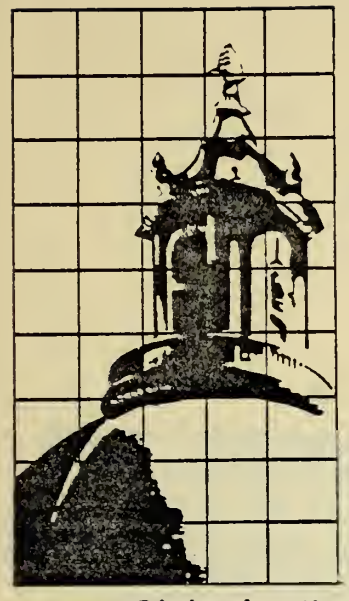
Timely Payment — A payment mechanism whereby a provider receives a check for 1/24th of the annual payment on the 15th day of the month after the services were provided. On the 30th day, another check for 1/24th is received. After the 30th, but prior to the 45th (15 days into month two), the provider submits a voucher showing actual expenses for the first 30 days. The purchasing agency adjusts the third 1/24th payment to reflect actual costs.

Unit-Rate Contract A contract that has as its payment basis the number of units of service delivered (see Unit of Service).

Unit of Service A measure of service rendered (e.g., an hour of counseling, a diagnostic report, a client evaluation, or a training session).

Vacancy Tracking A system that provides up-to-the-minute information on the availability of open beds or vacant slots in the contracted programs.

Vendor In the social service industry, an entity that contracts with the Commonwealth to provide mental health, social, or rehabilitative services (see Provider).



Chapter VII
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